

November 21, 2005

Via Electronic Mail (rule-comments@sec.gov)

Mr. Jonathon G. Katz, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

**Re: File No. S7-09-05 – Commission Guidance Regarding Client
Commission Practices Under Section 28(e) of the Securities and
Exchange Act of 1934, SEC Release No. 34-52635 (October 19, 2005)**

Dear Mr. Katz:

Capital Institutional Services, Inc. (“CAPIS”) appreciates the opportunity to comment on the Securities and Exchange Commission’s (“SEC”) interpretive release on Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934. With over 28 years experience and as one of the largest remaining independent broker-dealers, CAPIS performs a valuable role in the industry by delivering a wide range of services and fostering competition in the industry. Our service offering is broad and includes global agency trading, advanced order execution and independent research distribution for asset managers and plan sponsors.

We believe the SEC’s interpretative release is a solid step in restoring industry confidence in a long-standing and valuable service that helps balance competition in the industry and supports the growth of smaller investment managers and research providers. Given that this subset of the industry is our primary base, CAPIS has actively participated in conversations regarding this practice to ensure that our views and those of our clients’ are represented and framed correctly.

As a broker/dealer, we are pleased to support the SEC's interpretation of Section 28(e), including the new concepts identified in the release regarding products and services allowable under the safe harbor. However, it is important to note that the fiduciary continues to have the ultimate obligation to determine what products and services are appropriate under the safe harbor.

Comments

- *Order Management Systems (OMS)*

We would suggest that further clarification is needed on the Commission's stance that OMSs are not allowable under brokerage services. As a guide to determining services allowed under brokerage, the SEC outlined a specific standard to be applied. This temporal standard, as it is defined¹ currently, would seem to allow, at least partially, OMSs as a brokerage service, as their use often fits clearly within the definition of the temporal standard. Furthermore, for those portions of the systems that may not be allowed as research or may fall outside the temporal standard, OMSs should simply be allocated on a mixed-use basis.

- *Commission Sharing Arrangements*

We request further clarification on the allowable commission sharing arrangements under Section 28(e). The SEC outlined four points to determine whether a commission sharing arrangement meets the standard to fall within the safe harbor. Our particular concern relates to the second point², in which the SEC states the introducing broker-dealer must make or maintain certain records.

The current standard for commission sharing arrangements maintains that both the introducing and clearing brokers must meet certain books and records requirements, but

¹ See Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934, p 34. "...we believe that brokerage begins when the money manager communicates with the broker-dealer for the purpose of transmitting an order for execution and ends when funds or securities are delivered or credited to the advised account or the account holder's agent."

² See Commission Guidance Regarding Client Commission Practices Under Section 28(e) of the Securities Exchange Act of 1934, p 46. "make and/or maintain records relating to its customer trades required by Commission and SRO rules, including blotters and memoranda of orders."

does not appear to require introducing brokers to create and maintain the types of records suggested in the Commission's proposed interpretive release. Specifically, blotters and memorandums of orders for each client have not been required to be maintained by introducing brokers. Therefore, we request that the Commission clarify this issue to confirm that the recent comments on this point were meant to reaffirm the logic currently set out by existing rule. Specifically, per SEC Rule 17a-3(b)(i), it remains acceptable for introducing brokers and clearing brokers to make and maintain the type of records outlined under the rule.

- *Implementation*

We believe it is critical that the SEC provide a reasonable transition period for firms to unwind existing third-party research contracts, rewrite and revisit existing commission sharing agreements and receive appropriate regulatory approval for said documents. CAPIS requests the SEC allow firms at least 12 months to implement new procedures once the formal interpretation is adopted. With regard to any contracts that may expire after such time, we request firms be allowed to let said contracts expire before applying the new rules set forth by the SEC.

- *Cross Regulation*

The SEC has taken considerable effort to maintain relative parity between its regulation and those proposed by the Financial Services Authority (FSA). Although similarities in international regulation provides a solid framework for what is allowable when using client commissions, there is one aspect in which further clarification would be appreciated. The primary difference noted between the FSA and the SEC is transparency. While the FSA has notably pushed for the unbundling of research costs from trade costs, the SEC has yet to provide specific guidance on this matter.

We look forward to the SEC's guidance on transparency as we believe it is key in achieving equal treatment of bundled and third party independent research. Further, we believe that such transparency is integral in order for investment managers to meet their obligation under Section 28(e). Specifically, the SEC has charged investment managers with ensuring the cost of research obtained with client commissions is justified in relation to the value it provides. Without transparency of bundled research, determination of research value relative to its cost may prove to be an overly burdensome task.

Conclusion

In summary, CAPIS believes the interpretive release on Client Commission Practices Under Section 28(e) affirms the value of acquiring products and services with commission dollars. The new concepts add important guidance on allowable practices and should help restore faith in the use of commission dollars to acquire legitimate products and services. This interpretation will enable investment managers to better understand how they can properly leverage client commissions in order to obtain appropriate research and brokerage services. Further, it likely will allow for more clearly focused regulatory scrutiny of the practice. In addition, the SEC's effort on this issue will encourage the growth and development of the burgeoning independent research community and help shape a market where research is judged on its merits and not by its provider.

Once again, we appreciate the opportunity to comment on this issue. If we can be of any further assistance or if we can clarify any issues discussed, please contact us.

Respectfully submitted,



Kristi P. Wetherington
President